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No.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

INNKEEPERS OF NEW CASTLE, INC.,
Petitioner.

vs.

ROBERT J. MALEY, ALEXANDER HAMILTON LIFE INSURANCE COMPANY OF AMERICA,
Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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QUESTIONS PRESENTED FOR REVIEW

1. Whether the Bankruptcy Court has the exclusive jurisdiction to supervise hiring of attorneys and the allowance of attorney fees in Chapter XI proceedings, 11 U.S.C. §§701-799 (1976)?[1]

2. Whether the Bankruptcy Court's authority to decide controversies regarding attorney fees is among the Article I powers of the Bankruptcy Court falling within the "summary jurisdiction" affirmed by the Supreme Court in *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, Nos. 81-150 & 81-546, slip op. (U.S. June 28, 1982)?

3. Whether choses in action of the debtor become assets of the estate upon the filing of a petition initiating a proceeding under the Bankruptcy Act?

4. Whether an order authorizing a debtor to proceed with State Court litigation subjects the whole of the litigation including the settlement and liquidation of an attorney's lien to the jurisdiction of a state court?

5. Whether federal bankruptcy law must be applied to the analysis of an attorney fee lien arising under state law?

6. Whether attorney fee contracts are entitled to the treatment generally afforded executory contracts

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[1]This case was commenced under the Bankruptcy Act of 1898 as amended [hereinafter cited as *Bankruptcy Act*]. Therefore, unless otherwise specifically stated, all citations are to the Bankruptcy Act and the United States Code provisions which parallel the Bankruptcy Act. *See Bankruptcy Reform Act of 1978*, Pub. L. No. 95-598 §403(a), 92 Stat. 2683 (1978). The Bankruptcy Act and parallel United States Code provisions have been repealed. *See Bankruptcy Reform Act of 1978*, Pub. L. No. 95-598 §401(a), 92 Stat. 2683 (1978). The Bankruptcy Rules cited were promulgated by the Supreme Court in 1973 pursuant to 28 U.S.C. 2075 (1976) (current version at 28 U.S.C. §2075 (Supp. IV 1980)) and continue in effect under the Bankruptcy Reform Act of 1978 to the extent the rules are not inconsistent with the Bankruptcy Reform Act of 1978. *See Bankruptcy Reform Act of 1978*, Pub. L. No. 95-598 §405(d), 92 Stat. 2683 (1978).

pursuant to Section 313 of the Bankruptcy Act, 11 U.S.C. §713 (1976)?

7. Whether the Bankruptcy Court possesses the jurisdiction to determine the extent, validity and priority of liens asserted against assets of the estate?

8. Whether the decision of the Court of Appeals is an erroneous substantial erosion of statutory and legal principle when it finds: (1) that a pre-filing attorney fee agreement is entitled to executory contract treatment pursuant to Section 313 of the Bankruptcy Act, 11 U.S.C. §713 (1976) and is not subject to review by the Bankruptcy Court under Bankruptcy Rules 215, 219 and 220; (2) that a cause of action owned by the debtor on the commencement of the bankruptcy proceeding is not an asset of the bankruptcy estate; (3) that notwithstanding Indiana statutory and legal principle, the filing of a notice of intention to assert a lien pursuant to Indiana Code §33-1-3-1 (1976) was conclusive in establishing lien validity and amount; (4) that where a valid attorney's lien is asserted for services rendered with respect to an asset of the estate, the Bankruptcy Court's right to review fees under Bankruptcy Rules 219 and 220 does not apply; and (5) that an order of the Bankruptcy Court authorizing the continuation of condemnation litigation by the debtor was a waiver of Bankruptcy Court jurisdiction and subjected the whole of the litigation including the settlement and liquidation of an attorney's lien charge to the jurisdiction of the state court?

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

Innkeepers of New Castle, Inc. prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Seventh Circuit entered on February 10, 1982.

OPINION BELOW

The opinion of the United States Court of Appeals for the

Seventh Circuit is reported at 671 F.2d 221 (7th Cir. 1982) and is set out in the Appendix at A-1. The order denying the petition for rehearing is unpublished but appears in the Appendix at A-55. The opinion and order for payment of attorneys' fees and allowances of the District Court for the Southern District of Indiana is unpublished but appears in the Appendix at A-24. The recommendations of Bankruptcy Judge on application for allowances is unpublished but appears in the Appendix at A-26.

JURISDICTION

The judgment of the Court of Appeals for the Seventh Circuit was entered on February 10, 1982. A timely petition for rehearing *en banc* was denied on March 10, 1982, and an application for extension of time in which to file petition for writ of certiorari was filed on May 28, 1982 with this Court. On May 28, 1982, this Court entered its order extending the time to file petition for writ of certiorari to and including August 7, 1982. This Court's jurisdiction is invoked under Section 24 of the Bankruptcy Act, 11 U.S.C. §47 (1976) and 28 U.S.C. §1254(1) (1976).

CONSTITUTIONAL PROVISIONS, STATUTES AND BANKRUPTCY RULES INVOLVED

This cases involves the United States Constitution, Article I, Section 8, clause 4 and the United States Constitution, Article III, which are set forth in the Appendix, A-56 to A-59.

The statutes involved in this case are the Bankruptcy Act of 1898, §§24a, 24c, 62d, 67c(1)(B), 70a(5), 70a(6), 70b, 306(4), 311, 313(1), 342, 357(2), and the parallel provisions of the United States Code of 1976, which are 11 U.S.C. §47(a), 11 U.S.C. §47(c), 11 U.S.C. §102(d), 11 U.S.C. §107(c)(1)(B), 11 U.S.C. §110(a)(5), 11 U.S.C. §110(a)(6), 11 U.S.C. §110(b), 11 U.S.C. §706(4), 11 U.S.C. §711, 11 U.S.C. §713(1), 11 U.S.C. §742, 11 U.S.C. §757(2), 28 U.S.C. §311

(1976), 28 U.S.C. §1254(1) (1976), 28 U.S.C. §2075 (1976);[2] and Indiana Code §33-1-3-1 (1976) all of which are set forth in the Appendix, A-59 to A-68.

The Rules of Bankruptcy Procedure involved in this case are Bankruptcy Rules 215, 219, 220, 10-206, 10-215, 10-217, 11-11, 11-22, 11-31 and 11-32, all of which are set forth in the Appendix, A-69 to A-80.

STATEMENT OF THE CASE

This matter originated with the filing of a petition for an arrangement under Chapter XI of the Bankruptcy Act pursuant to 11 U.S.C. §§701-799 (1976)[3] by the debtor, Innkeepers of New Castle, Inc. The District Court's jurisdiction over the cause exists pursuant to Section 311 of the Bankruptcy Act, 11 U.S.C. §711 (1976). A final "Order of Court for Payment of Attorneys' Fees and Allowances" was entered by the District Court on December 11, 1980. Appeals taken from that order to the Court of Appeals for the Seventh Circuit were pursuant to Section 24a of the Bankruptcy Act, 11 U.S.C. §47(a) (1976).

On November 17, 1976, Innkeepers filed its "Original Petition under Chapter XI" commencing the proceedings. On the same date, Innkeepers filed its "Application to Employ Counsel"[4] wherein the debtor sought to retain Robert Maley and the law firm of Bamberger & Feibleman to, among other matters, "perform all other legal services for debtor as debtor-in-possession which may be necessary to protect debtor's interests and successfully obtain the object of debtor's Chapter XI proceedings."[5] Pursuant to said application, on the same date, the Bankruptcy Court entered its order authorizing the appointment of Robert

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[2] *See supra* note 1.
[3] *See supra* note 1.
[4] Record, Vol. 1 at 89.
[5] Record, Vol. 1 at 90.

Maley and the firm of Bamberger & Feibleman as attorneys on general retainer.[6]

On December 6, 1976, Innkeepers filed its application to go forward with a certain condemnation action entitled *State of Indiana v. Innkeepers of New Castle, Inc.*, then pending in the Fayette County, Indiana, Circuit Court. Said application alleged that "funds generated from said lawsuit form the basis for a portion of the plan of arrangement to be proposed herein."[7] On the same day, the Bankruptcy Court entered an order authorizing the same.

On December 8, 1976, following a jury trial, a judgment in favor of Innkeepers in the amount of $1,135,254.79 was entered in the condemnation action. On the same day, without notice to the Bankruptcy Court, pursuant to Indiana Code §33-1-3-1 (1976), Robert J. Maley and local counsel, Jim C. Cordes, entered in writing upon the judgment docket in Fayette County, Indiana notice of their intention to hold a lien on proceeds of the judgment for the amount of their attorneys fees claim which they alleged to be the sums of $567,637.00 and $100,000.00, respectively. Robert Maley's claim for the sum of $567,637.00 was based upon an oral contingent fee contract of employment between his firm and Innkeepers entered into in April 1971 and memorialized in writing on January 5, 1976 whereby Maley's firm was entitled to fifty percent of any recovery subject to minor adjustments. Jim Cordes's claim was based upon services rendered.

The existence of the contingent fee contract of Maley and the employment of Cordes was never disclosed to the Bankruptcy Court until the filing of their applications for allowances with the Bankruptcy Court in 1979. The only reference with respect to Innkeepers's pre-filing obligation

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[6]Record, Vol. 1 at 91.

[7]Record, Vol. 1 at 93.

to Maley for fees is contained in the Innkeepers's statement of affairs which was filed in the proceeding on December 21, 1976 after the condemnation judgment was entered and the attorneys lien was asserted and which states "Fees for legal services in 1976—bill not rendered (State of Indiana v. Innkeepers of New Castle, Inc.—50% of amount recovered over costs.)"[8] Neither the contingent fee contract of Maley nor Mr. Cordes's employment agreement were disclosed in the Statement of Executory Contracts filed by the debtor pursuant to Bankruptcy Rule 11-11 on December 31, 1976.[9] Neither Mr. Maley nor Mr. Cordes disclosed the existence of the employment contracts by affidavit as required by Bankruptcy Rule 219.

By entry dated March 28, 1977, the Bankruptcy Court determined that mortgage lenders Alexander Hamilton Life Insurance Company of America and Citizens State Bank of New Castle, Indiana possessed valid and enforceable liens upon the condemnation judgment proceeds to the same extent and amount and with the same relative priority as their mortgages constitute valid and enforceable liens.[10] By order dated November 7, 1979, the Bankruptcy Court directed that the condemnation judgment proceeds be invested by Innkeepers and that the liens of the mortgage lenders and the "asserted liens" of Robert Maley and James C. Cordes attach to proceeds to the same extent as if those funds remained in the possession of the Clerk of the Fayette County Circuit Court. That order further provides that "the extent, validity and priority of all liens asserted against proceeds shall be determined by this Court after notice and actual hearing."[11]

On November 15, 1979, the Bankruptcy Court ordered the attorneys asserting liens on the condemnation

[8]Record, Vol. 1 at 57.
[9]Record, Vol. 1 at 81-84.
[10]Record, Vol. 1 at 99.
[11]Record, Vol. 1 at 111.

judgment to file their applications for attorneys fees in connection with the judgment.[12] Cordes filed his application for payment of attorney fees on November 30, 1979.[13] On December 7, 1979, Maley filed his application for attorney fees wherein he moved "the Court to order the debtor-in-possession to pay the attorney fees due him for his services as attorney for debtor-in-possession...."[14] Objections to the applications were filed on December 13, 1979, by Alexander Hamilton and Citizens State Bank of New Castle, Indiana.

Pursuant to notice, a hearing was held and on July 24, 1980 the Bankruptcy Judge entered his "Recommendations of Bankruptcy Judge on Applications for Allowances," wherein the Bankruptcy Judge held, *inter alia*, that the Bankruptcy Court has paramount and exclusive jurisdiction to determine attorney fee allowances and exclusive jurisdiction over all property of the estate including the proceeds of the condemnation judgment; that Maley and Cordes failed to comply with Section 62d of the Bankruptcy Act, 11 U.S.C. §102(d) (1976) and Bankruptcy Rule 219(b) covering disclosure of compensation paid and promised and division of compensation; that the Bankruptcy Court is not bound by the contingent fee agreement, but is obligated to make reasonable allowances of attorney fees taking into consideration such factors as economy, benefit to creditors, efficiency, the size of the estate and the proportionate amount thereof recovered through the efforts of the attorney, the time expended by the attorney, attorney's ability and experience, difficulty and intricacy of the legal propositions determined, evidence in the record of the reasonableness of the fee and the total cost incurred in the administration of the estate as related to the size thereof. The Court further found that the

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[12]Record, Vol. 1 at 115.
[13]Record, Vol. 1 at 118.
[14]Record, Vol. 1 at 190.

Bankruptcy Court had the jurisdiction to determine validity of the attorneys lien, although there was no need to do so in the instant cause since attorney fees allowed would be administration expenses and would have a first priority against funds of the estate.[15]

With respect to the allowance of fees for Jim C. Cordes, the Bankruptcy Judge found that employment of Cordes had never been approved by the Bankruptcy Court; that Cordes had been retained by Maley and that because the Court did not make any arrangement for local counsel it was not obligated to calculate a separate award. Further, because there was no itemization of services upon which to make a calculation for Cordes, the Bankruptcy Judge determined that Cordes and Maley should decide among themselves how the fee should be split. The Court then recommended that a "fair and reasonable" allowance to Maley and Cordes was the sum of $325,000.00.[16]

On December 11, 1980, the District Court for the Southern District of Indiana adopted the recommendations of the Bankruptcy Judge, followed the principle set out in *Massachusetts Life Insurance Company v. Brock*, 405 F.2d 429, 432-433 (5th Cir. 1968) wherein the Court said:

> The public interest which is inherent in bankruptcy matters must be considered in awarding fees. The object is to draw a balance to the end that competent trustees and counsel are obtainable...[and]...fairly compensated...while at the same time doing equity to the debtor and creditors.

and allowed Maley and Cordes a combined fee of $325,000.00.[17]

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[15]The Bankruptcy Court's Recommendations for Allowances appears in the Appendix, A-26.

[16]*See supra* note 15.

[17]The decision of the District Court appears in the Appendix, A-24.

On appeal, the order of the District Court was affirmed by the Court of Appeals insofar as it awarded Maley recovery of expenses and repaid witness fees advanced, and reversed insofar as the District Court's order fixed Maley's fee in the amount of $325,000.00 to be shared with Cordes. In addition, the cause was remanded to the District Court with instructions to hold an evidentiary hearing to determine the net recovery due Innkeepers from the condemnation proceedings and to award to Maley fifty percent of the net recovery pursuant to his perfected attorney's lien and his contingent fee contract together with fifty percent of the post-condemnation judgment interest earned by Innkeepers. Further, the District Court was instructed to compute the proper amount in settlement and discharge of Cordes's lien on a *quantum meruit* basis and was instructed to set aside that sum together with his pro rata share of the post-condemnation judgment interest earned by Innkeepers. The balance of the net recovery and interest was to be set aside to the estate.[18]

The Court of Appeals decision was based upon the following grounds:

1. That the contingent fee contract was an executory contract "which was not rejected by the debtor, any creditor or the Court, *sua sponte*," and is therefore binding upon the Court and the parties.

2. That Maley only represented the "debtor" as opposed to the "debtor-in-possession" and that pursuant to the Bankruptcy Court's order of December 6, 1976, Maley pursued the condemnation action to its completion only on behalf of the "debtor" and not the "debtor-in-possession," therefore the asset was retained by the "debtor" and managed apart from the bankruptcy estate. Consequently, the validity of his contingent fee contract and the validity and amount of Maley's attorneys lien could not be questioned by the Bankruptcy Court.

[18]The opinion of the Court of Appeals appears in the Appendix A-1.

3. That the Bankruptcy Court's order of November 28, 1977 sequestering the proceeds of the condemnation proceedings deprived the state court of its prerogative to determine the validity of the attorneys lien.

4. That the filing of notice of intention to assert a lien pursuant to Indiana Code 33-1-3-1 (1976) was conclusive in establishing that Maley's attorneys lien was a valid lien in the amount called for by his contingent fee contract.

5. That Bankruptcy Rules 219 and 220 are not applicable because the estate's chose in action was encumbered by a valid attorneys lien which could not be questioned in the bankruptcy proceeding.

6. That the order of December 6, 1976 subjected the whole of the condemnation litigation including the settlement and liquidation of the attorneys lien charge to the jurisdiction of the state court because by that order the Bankruptcy Court relinquished "summary jurisdiction" and that, therefore, the Bankruptcy Court could not consider the validity or amount of the attorneys lien.

REASONS FOR GRANTING THE WRIT

1. The Court of Appeals decision conflicts with the mandate of Bankruptcy Rules 215 and 219 as promulgated by the Supreme Court and with the principle of Supreme Court holdings as to the jurisdiction and power of the Bankruptcy Court to supervise the hiring of attorneys and the allowance of attorneys fees.

The Supreme Court of the United States has the power to prescribe rules for carrying out the provisions of the Bankruptcy Act.[19] 28 U.S.C. §2075 (1976). Among the rules so promulgated is Bankruptcy Rule 11-22 which makes Bankruptcy Rule 215 applicable in Chapter XI cases to the employment of attorneys for the debtor-in-possession.

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[19] *See supra* note 1.

Bankruptcy Rule 215 provides that no attorney for a debtor-in-possession "shall be employed except upon order of the Court."

Bankruptcy Rule 11-31 makes Bankruptcy Rule 219 applicable in Chapter XI cases. Bankruptcy Rule 219(a) states in part:

> *Application for Compensation or Reimbursement.* A person seeking compensation for services or reimbursement of necessary expenses...shall file with the court an application....

Bankruptcy Rule 219(b) states in part:

> *Disclosure of Compensation Paid or Promised to Attorney for Bankrupt.* Every attorney for a bankrupt, whether or not he applies for compensation, shall file with the court on or before the first date set for the first meeting of creditors...a statement setting forth the compensation paid or promised him for the services rendered or to be rendered in connection with the case, [and] the source of the compensation so paid or promised....

Bankruptcy Rule 219(c) states in pertinent part:

> *General.* The compensation allowable by the court to [an]...attorney...for services rendered in the administration of a bankrupt estate shall be reasonable, and in making allowances the court shall give due consideration to the nature, extent, and value of services rendered as well as to the conservation of the estate and the interests of creditors....

The language of those rules is unequivocal and unambiguous. Their effect is pervasive: (1) *No* attorney for the debtor may be employed without court approval, (2) *all* agreements for compensation must be disclosed to the Court, (3) *a person* seeking compensation *must* file with the Court an application for fees, and (4) compensation allowable by the Court *must be reasonable.*

Rules 215 and 219, with others, represent the cumulative experience of Congress and the federal courts over a period of nearly one hundred years wherein the regulation of costs and fees in bankruptcy proceedings has been a matter of continuing concern. By these rules, the Bankruptcy Court has been granted the unquestioned authority and absolute obligation to review and make allowances of all attorney fee claims in an estate arising from the bankruptcy proceedings. That view is consistent with Section 62d of the Bankruptcy Act, which Rule 219 replaces, and decisions of this Court which have uniformly upheld the jurisdiction and power of the Bankruptcy Court to review and allow attorney fee claims. *Katchen v. Landy*, 382 U.S. 323 (1966); *Leiman v. Guttman*, 336 U.S. 1 (1948); *Brown v. Gerdes*, 321 U.S. 178 (1944); *Conrad, Rubin & Lesser v. Pender*, 289 U.S. 472 (1933); *Watkins v. Sedberry*, 261 U.S. 571 (1923); *In re Wood & Henderson*, 210 U.S. 246 (1908).

The Advisory Committee on Bankruptcy Rules, established pursuant to 28 U.S.C. §331 (1976), discussed the duties and responsibilities of the Bankruptcy Court with regard to the granting of compensation in its notes to Rule 219. The Committee stated:

> The premise for including in these rules provisions governing the allowance of compensation to officers, attorneys, and accountants is that it is peculiarly a judicial responsibility to supervise the administration of estates and in particular to assure that allowances for compensation to those rendering services in connection therewith are fair but not excessive. 3A Collier ¶62.05[3] (1961). The costs of bankruptcy administration have been a matter of continuing concern in the history of American bankruptcy law. Id. ¶62.02. This concern has led to an increasing recognition of the necessity for close judicial control of these costs.

Advisory Committee Note on Bankruptcy Rules 219, reprinted in 12 COLLIER ON BANKRUPTCY ¶219.01 at 2-206 (14th ed. 1978).

As stated by the Court in *Carter v. Wood*, 433 F.Supp. 291 (W.D. Mo. 1977), at 294 in discussing the Advisory Committee's Note to 219:

> These concerns, together with the general policy in the Bankruptcy area against any "transfer of judicial power over expenditure and allowances from the court to persons who, at best, have a distinctly lesser degree of public responsibilities," 3A Collier ¶62.37, p. 1637 (1961), make clear that the law does not permit a Bankruptcy Court to contract away its obligation, under the law, to grant only reasonable compensation to attorneys for their services rendered in the administration of a bankrupt estate.

The Court of Appeals in the instant case has totally ignored the existence of Bankruptcy Rule 215 and found that Bankruptcy Rule 219 was not applicable because of a variety of distinguishing factors all arising as the result of the existence of the pre-petition contingent fee contract. The mandate of the applicable bankruptcy rules makes such differentiation inappropriate. At best, the contract could only be evidence of what a reasonable fee could be, it could never be determinative since Bankruptcy Rule 219 imposes upon the Court the duty to assure that no other than a reasonable fee be paid to attorneys in bankruptcy proceedings irrespective of the contractual basis of the fee requested. *Carter v. Wood*, 433 F.Supp. 291 (W.D. Mo. 1977).

None of the legal principles addressed have been affected by the Bankruptcy Reform Act of 1978 and the issue remains relevant under current law. No court should be allowed to ignore rules promulgated by the Supreme Court. It is imperative to the economical and orderly administration of Chapter XI estates that this Court reaffirm, in light of its Bankruptcy Rules 215 and 219, the exclusive jurisdiction and power of the Bankruptcy Court to supervise the hiring of attorneys and the allowance of attorneys fees in Chapter XI proceedings.

2. The Bankruptcy Court's authority to decide controversies regarding attorney fees is among the Article I powers of the Bankruptcy Court falling within the "summary jurisdiction" affirmed by the Supreme Court in *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*

Justice Brennan, writing for the plurality in *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, Nos. 81-150 & 81-546, slip op. (U.S. June 28, 1982), stated that prior to the adoption of the Bankruptcy Act of 1978:

> The Bankruptcy Courts were vested with 'summary jurisdiction'—that is, with jurisdiction over controversies involving property in the actual or constructive possession of the Court.

Id at 2.

He proceeded to describe the important enlargement of jurisdiction under the Bankruptcy Reform Act of 1978 as follows:

> The jurisdiction of the bankruptcy courts created by the Act is much broader than that exercised under the former referee system. Eliminating the distinction between 'summary' and 'plenary' jurisdiction, the Act grants the new courts jurisdiction over all 'civil proceedings arising under title 11 [the Bankruptcy title] or arising in or *related to* cases under title 11.' (citations omitted.)

Id at 2-3.

Implicit in the decision of the plurality are the conclusions that, "the restructuring of debtor-creditor relations, which is at the core of the federal bankruptcy power," slip op. at 20-21, and "the manner in which the rights of debtors and creditors are adjusted," *id* at 34 n. 36, form the basis of the Congressional grant to the Bankruptcy Courts.

Nothing in the plurality decision can be found to disturb the traditional jurisdiction of Bankruptcy Courts over the manner in which the rights of debtors and creditors are adjusted. In this conclusion the minority appears to agree. Justice White, in his characterization of the plurality opinion writes: "Under the plurality's own interpretation of the cases, therefore, these matters could be heard and decided by Article I judges." Slip op. at 4 (White, J. dissenting).

The dispute between the plurality and dissent in *Northern Pipeline Construction Co.* revolves to some extent around the incompletely resolved issue of the extent to which the Bankruptcy Act of 1978 exceeded the constitutionally permissible grant of summary jurisdiction originally vested in the bankruptcy courts by Congress. Central to the resolution of the issues presented in this case is the concept of the limits of the summary jurisdiction available to the bankruptcy courts.

Both the plurality, in note 31 at page 29, and the dissent, at page 8, in *Northern Pipeline Construction Co.* acknowledge the importance of the Court's prior decision in *Katchen v. Landy*, 382 U.S. 323 (1966), which established the parameters of summary jurisdiction in the Bankruptcy Courts as of 1966. However, the plurality clearly notes in its reference to *Katchen* that "when *Katchen* was decided the 1973 Bankruptcy rules had not yet been adopted...." and that in the decision "there was no discussion of the Article III issue." Slip op. at 29 n. 31.

The questions presented in this appeal provide the Court with a unique opportunity to update the *Katchen* discussion of summary jurisdiction in the Bankruptcy Courts with reference to, and in light of, the Article III issue. U.S. CONST., art. III.

The instant case involves an attorney who submitted himself to the jurisdiction of the Bankruptcy Court but claims that the amount of attorney fees which should be

allowed must be determined only by reference to state law, contract law and considerations outside the jurisdiction of the Bankruptcy Court.

Further, the Court of Appeals relies on the 1938 Second Circuit case of *In re Prudence Co.*, 96 F.2d 157, to support its contention that the Bankruptcy Court's jurisdiction does not extend to a determination of attorneys fees. The *Prudence* decision predates the 1973 Bankruptcy Rules promulgated by this Supreme Court and referred to in note 31 at page 29 of the *Northern Pipeline Construction Co.* decision.

Rules 219 and 220 of the Bankruptcy Rules both implicitly overrule the *Prudence* decision which restricts even the Article I summary jurisdiction of the Bankruptcy Courts. U.S. CONST. art. I, §8, cl. 4. The revival of the *Prudence* decision by the Seventh Circuit Court of Appeals decision below is of exceptional importance because that decision has impermissibly stripped the Bankruptcy Court of its jurisdictional duties to supervise the bankruptcy estate including the disallowance of unreasonable attorney fees, all of which the Bankruptcy Courts have been specifically authorized to do by the United States Supreme Court pursuant to Bankruptcy Rules 219 and 220.

The decision of the Court of Appeals in the instant case purports to limit what the court in its decision characterizes as the "exclusive summary jurisdiction" of the Bankruptcy Courts. The court states that:

> Bankruptcy courts are subject to some limitation in the exercise of their summary jurisdiction in circumstances such as those presented here.

671 F.2d at 230 *reprinted in* Appendix at A-1.

It must be noted that nowhere in the United States Supreme Court's discussion of summary jurisdiction in the *Katchen* decision or in prior discussions of bankruptcy

attorney fees in *Watkins v. Sedberry*, 261 U.S. 571 (1923), or *Brown v. Gerdes*, 321 U.S. 178 (1944), is a similar conclusion reached. In fact, Bankruptcy Rules 219 and 220 promulgated by the Supreme Court lead to an entirely opposite conclusion.

This case presents the Supreme Court with a rare opportunity to clarify questions of law implicitly raised by, but outside the scope of, the specific constitutional findings of the recent *Northern Pipeline Construction Co.* decision. Petitioner urges this Court to grant certiorari and address the important issues raised in this appeal.

3. The Court of Appeals as a matter of first impression and erroneously decided that a contract for attorneys fees entered into by the debtor and his counsel prior to the commencement of Chapter XI proceedings is entitled to the treatment generally afforded executory contracts pursuant to Bankruptcy Act Section 313 and Section 357(2), and is not subject to review by the Bankruptcy Court pursuant to the provisions of Bankruptcy Rules 215 and 219, which determination is one that is significant and reoccurring and has not been, but should be, decided by this Court.

Section 70b,[20] 313(1),[21] and 357(2)[22] of the Bankruptcy Act form the basis of the debtor's duty and privilege to reject executory contracts of the debtor. What constitutes an executory contract is not specifically defined by the Act. Bankruptcy Act §306(4), 11 U.S.C. §706(4) (1976). While it is an ambiguous term, it has generally been held to embrace contracts dealing with any subject matter as long as some future performance is required of the debtor. 8 COLLIER ON BANKRUPTCY, ¶2.10 at 84-86 (14th ed. 1978).

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[20] 11 U.S.C. §110(b) (1976).
[21] 11 U.S.C. §713(1) (1976).
[22] 11 U.S.C. §757(2) (1976).

The Court of Appeals determined that the contingent fee contract in question was an executory contract which was affirmed by nonaction on the part of the debtor, any creditor or the Court, and, therefore, the Court and the parties were bound by its terms. That being the case, Bankruptcy Rule 219 was not applicable.

Petitioner agrees that the contingent fee contract was an executory contract as contemplated by the definition of the term under the Bankruptcy Act. In fact, all attorneys fee contracts where future services are required in proceedings under the Act are executory if entered into prior to the commencement of the proceedings including the contract of employment between every debtor and his reorganization counsel in every case. The Court of Appeals decision is, therefore, precedent for a proposition of first impression: That every attorney fee contract entered into prior to the commencement of a proceeding is binding upon the Court and not subject to review unless the fee agreement is first affirmatively rejected.

That proposition, for which the Court of Appeals cites no authority, is without foundation in law because it ignores the special relationship between attorney and client that has resulted in the promulgation of special rules to govern that relationship in bankruptcy proceedings. The law of executory contracts is not applicable to attorney fee contracts, the law of Bankruptcy Rules 215, 219 and 220 is controlling.

The mandate of Bankruptcy Rules 215, 219 and 220 is absolute. Those rules impose upon the Court the duty to assure that no other than a reasonable fee be paid to attorneys in bankruptcy proceedings irrespective of the contractual basis of the fee requested. *Carter v. Wood*, 433 F.Supp. 291 (W.D. Mo. 1977).

The Advisory Committee on Bankruptcy Rules, established pursuant to 28 U.S.C. §331 (1976), discussed the duties and responsibilities of the Bankruptcy Court with

regard to the granting of compensation in its notes to Rule 219. The Committee stated:

> The premise for including in these rules provisions governing the allowance of compensation to officers, attorneys, and accountants is that it is peculiarly a judicial responsibility to supervise the administration of estates and in particular to assure that allowances for compensation to those rendering services in connection therewith are fair but not excessive. 3A Collier ¶62.05[3] (1961). The costs of bankruptcy administration have been a matter of continuing concern in the history of American bankruptcy law. Id. ¶62.02. This concern has led to an increasing recognition of the necessity for close judicial control of these costs.[23]

As stated by the Court in *Carter v. Wood*, 433 F.Supp at 294 in discussing the Advisory Committee's Note to 219:

> These concerns, together with the general policy in the Bankruptcy area against any "transfer of judicial power over expenditure and allowances from the court to persons who, at best, have a distinctly lesser degree of public responsibilities," 3A Collier ¶62.37, p. 1637 (1961), make clear that the law does not permit a Bankruptcy Court to contract away its obligation, under the law, to grant only reasonable compensation to attorneys for their services rendered in the administration of a bankrupt estate.

None of the legal principles addressed have been affected by the Bankruptcy Reform Act of 1978 and the issue raised remains relevant under current law.

The finding that attorney fee agreements between a debtor and his counsel are entitled to the treatment generally afforded executory contracts and are binding upon the Court unless specifically rejected makes Bankruptcy Rules 215 and 219 inapplicable to virtually

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[23] *Advisory Committee on Bankruptcy Rules. Note to Bankruptcy Rule 219 reprinted in* 12 COLLIER ON BANKRUPTCY ¶219.01 at 2-206.

every attorney fee arrangement between a debtor and his counsel in bankruptcy proceedings and is an extremely important proposition that should be addressed by this Court.

4. **The Court of Appeals erroneously determined that an order of the Bankruptcy Court authorizing a debtor to proceed with pending state court litigation is a waiver of the Bankruptcy Court's exclusive jurisdiction to determine allowance of attorney fees which determination is one that is significant and reoccurring and has not been, but should be, decided by this Court.**

At the time of the commencement of the proceeding, the debtor was a party to a condemnation action pending in the Circuit Court of Fayette County, Indiana. On December 6, 1976, the debtor filed "Debtor's Application for Authority to Go Forward with Litigation" and on the same day the Court entered its order authorizing the debtor to do so. The Court of Appeals found that by entering the order, the Bankruptcy Court relinquished its jurisdiction to the state court to determine all matters arising out of the condemnation litigation including the extent and validity of the attorney's lien charge. In arriving at its conclusion, the Court of Appeals relied solely upon the authority of *Sherman v. Buckley*, 119 F.2d 280 (2nd Cir. 1941), *cert. denied* 314 U.S. 657.

While *Sherman v. Buckley* may be authority under its specific facts for the proposition advanced, it is clear that the holding is no longer, if it ever was, applicable to Chapter XI proceedings.

In *Brown v. Gerdes*, 321 U.S. 178 (1944), the Supreme Court granted a writ of certiorari in a case similar to the situation before us except that it involved a Chapter X proceeding. The Bankruptcy Court authorized the debtor to commence an action in the New York Courts to enforce

and collect claims against former officers and directors. It also authorized the retention of attorneys to pursue the suit as was the respondent, Maley, in the instant case. In 1941, before final judgment, the attorneys were discharged. Those attorneys proceeded to bring an action in the state court to fix and enforce their liens which the state court proceeded to do. The Supreme Court found that the power to determine the amount of fees rested solely with the Bankruptcy Court after reviewing all of the sections of the Bankruptcy Act concerning Chapter X proceedings which were applicable. In discussing *Sherman v. Buckley*, this Court stated:

> Whether that case was correctly decided on its facts we need not stop to inquire. It is sufficient to say that it does not state the correct rule of law under Ch. X of the Act.

Brown v. Gerdes, 321 U.S. at 184.

Since the *Brown v. Gerdes* decision in 1944, the law with respect to the bankruptcy court's exclusive jurisdiction to review and determine attorney fee allowances has continued to evolve through subsequent amendments to the Bankruptcy Act, the promulgation of Bankruptcy Rules and court decision. The thrust of the evolution has been uniformly to support the court's exclusive jurisdiction.

Bankruptcy Rules 215, 219 and 220 which are made controlling by Rules 11-22, 11-31 and 11-32 with respect to the review and allowance of fees in Chapter XI cases are nearly identical to Chapter X Rules 10-206, 10-215, and 10-217; and those rules all follow the direction of the law as espoused by this Court in *Brown v. Gerdes*, 321 U.S. 178 (1944). As a result, *Sherman v. Buckley* no longer states the correct rule of law under Chapter XI of the Bankruptcy Act, if, in fact, it ever did. *See also Katchen v. Landy*, 382 U.S. 323 (1966).

Bankruptcy Rules 215, 219 and 220 were not affected by the enactment of the Bankruptcy Reform Act of 1978. The

issue of whether an order of the Bankruptcy Court is a waiver of the Court's exclusive jurisdiction to determine allowances of attorneys fees is a significant and reoccurring question in all bankruptcy cases which should be addressed by this Court.

5. The decision below conflicts with the decisions of other United States Courts of Appeal as to the issue of the Bankruptcy Court's jurisdiction to determine the validity and amount of attorneys fees where the attorney's claim involves a separate contract or lien.

The Court of Appeals in the instant case cited the Second Circuit case of *In re Prudence Co.*, 96 F.2d 157 (2nd Cir. 1938) in support of its conclusion that "[b]ankruptcy courts are subject to some limitations in the exercise of their summary jurisdiction in circumstances such as those presented here."[24]

The Court of Appeals further cites the later Second Circuit case of *Sherman v. Buckley*, 119 F.2d 280 (2nd Cir. 1941), *cert. denied* 314 U.S. 657, for the proposition that the order of the Bankruptcy Court allowing the debtor-in-possession to proceed with a state court lawsuit "subjected the whole of the litigation, including the settlement and liquidation of the attorney's lien charge based on Maley's contract, *to the jurisdiction of the state court.*" (Court of Appeals' emphasis.)[25]

Although the petitioner contends that neither *In re Prudence Co.* nor *Sherman v. Buckley* generally support the conclusions reached by the Court of Appeals, to the extent that the Seventh Circuit has relied upon them to reach its findings there now exists a substantial conflict with the decisions of other circuits and within the Seventh Circuit itself.

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[24]Appendix at A-19.

[25]Appendix at A-15.

No other circuit has found the summary jurisdiction of the Bankruptcy Courts to be "subject to some limitations" in a factual circumstance where jurisdiction to determine the validity and amount of a contractual or lien-based attorney fee claim has been at issue.

The Eighth, Ninth and Tenth Circuits have generally held that the jurisdiction conferred on Bankruptcy Courts to fix the compensation of counsel is paramount and exclusive in similar factual circumstances. *In re Pacific Far East Line, Inc.*, 654 F.2d 664 (9th Cir. 1981); *Sanders v. Providence Washington Insurance Co.*, 442 F.2d 461 (8th Cir. 1971); *Jacobowitz v. Double Seven Corp.*, 378 F.2d 405 (9th Cir. 1967); *Official Creditors Committee of Fox Markets v. Ely*, 337 F.2d 461 (9th Cir. 1964); *Jackson v. Vance*, 179 F.2d 154 (10th Cir. 1949).

In addition, the instant decision is in direct conflict with a substantially similar case decided by the Seventh Circuit, namely, *In re Land Investors*, 554 F.2d 925 (7th Cir. 1976).

None of the legal principles addressed have been affected by the Bankruptcy Reform Act of 1978.The issue remains relevant and these conflicts justify the grant of certiorari to review the judgment below.

6. The decision below erroneously determined that a chose in action does not become an asset of the bankruptcy estate upon commencement of a bankruptcy proceeding in conflict with Sections 70, 311 and 342 of the Bankruptcy Act, and, further, the decision creates without precedent a separate entity called "the debtor" who may retain assets and administer them outside the jurisdiction of the Bankruptcy Court.

The Court of Appeals found that Maley never performed any legal services for the *debtor-in-possession*,[26] that the

[26]Appendix at A-16.

Bankruptcy Court erroneously considered Maley's legal services as being "services for Innkeepers as *debtor-in-possession* rather than for Innkeepers in its pre-Chapter 11 [sic] status and thereafter in the status as *debtor*";[27] that utilization of the factors normally considered in determining the reasonableness of attorneys fees "was reversible error because Maley's services were not rendered as part of the bankruptcy proceedings...."[28] Therefore, the Bankruptcy Court had no authority to review Maley's fee contract.

The finding of the Court of Appeals is clearly erroneous and has no foundation in law. Pursuant to Sections 70a(5) and 70a(6) of the Bankruptcy Act,[29] a trustee is vested with the bankrupt's title to all choses in action on the date of filing of the petition initiating the proceeding. Section 342 of the Bankruptcy Act[30] provides that where no trustee is appointed, the debtor shall continue in possession of his property and have all of the powers of the trustee, subject to the control of the court. Section 311 of the Bankruptcy Act[31] vests the Bankruptcy Court in a Chapter XI proceeding with exclusive jurisdiction of the debtor and his property wherever located.

Upon the filing of the proceeding, title to the chose in action passed to the debtor-in-possession by operation of law subject to the Court's exclusive jurisdiction. The "debtor," as the term is used by the Court below, no longer owned or possessed an interest in litigation for Maley to conduct. *See* 8 COLLIER ON BANKRUPTCY ¶6.32 at 928 (14th ed. 1978).

The decision of the Court below establishes precedent for the proposition that in a Chapter XI proceeding the "debtor" is a separate entity from the "debtor-in-

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[27]Appendix at A-16.
[28]Appendix at A-17.
[29]11 U.S.C. §110(a) (5) (1976) and 11 U.S.C. §110(a) (6) (1976).
[30]11 U.S.C. §742 (1976).
[31]11 U.S.C. §711 (1976).

possession" who may retain assets and administer them apart from the bankruptcy estate and outside the supervision of the Bankruptcy Court. The proposition is without legal precedent, potentially raises significant and reoccurring problems in the administration of Chapter XI proceedings and, inasmuch as the principles espoused by Sections 70(a), 311, and 342 were not altered by the Bankruptcy Reform Act of 1978, should be addressed by this Court.

7. The decision below fails to properly apply both Indiana law and applicable bankruptcy law to the analysis of a lien not perfected on the date of the commencement of the bankruptcy proceeding.

The Seventh Circuit opinion finds that Maley possessed a valid statutory attorney's charging lien against a judgment rendered for the debtor after the Chapter XI filing in a state court property condemnation action. The decision of the Court of Appeals completely fails to analyze the nature of respondent's alleged lien with reference to applicable bankruptcy law or state law.

The relevant section of the Bankruptcy Act is Section 67c(1)(B), 11 U.S.C. §107(c)(1)(B) (1976), which states in appropriate part that:

> The following liens shall be invalid against the Trustee:
>
> Every statutory lien which is not perfected or enforceable at the date of bankruptcy against one acquiring the rights of a bona fide purchaser from the debtor on that date, whether or not such purchaser exists: *Provided*, That where a statutory lien is not invalid at the date of bankruptcy against the trustee under subdivision (c) of Section 70 of this act and is required by applicable lien law to be perfected in order to be valid against a subsequent bona fide purchaser, such a lien may nevertheless be valid under this subdivision if perfected within the time permitted

> by and in accordance with the requirements of such law....

Without addressing, dismissing, or distinguishing Section 67c(1)(B), 11 U.S.C. §107(c)(1)(B) (1976), the Court of Appeals in the instant case held that the chose in action proceeds were encumbered with the perfected attorney's lien charges for Maley's services pursuant to his fully executed fee contract.

Maley's claim to a statutory lien arises from Indiana Code §33-1-3-1 (1976) which reads as follows:

> An attorney practicing his profession in any court of record in this State, shall be entitled to hold a lien, for his fees, on any judgment rendered in favor of any person or persons employing such attorney to obtain the same: Provided, That such attorney, within sixty (60) days from the time such judgment shall have been rendered, enter in writing upon the docket or record wherein the judgment is recorded, his intention to hold a lien thereon, together with the amount of his claim, and if an appeal is taken on such judgment, such lien shall be entered within sixty (60) days from the date the opinion of the higher court is recorded in the office of the Clerk of the trial court or from the date of final judgment wherein the cause is reversed and retried.

Indiana law is clear in that the cited statute is not applicable unless and until a judgment is obtained. *Kuhns v. Bech*, 147 Ind. 137, 45 N.E. 601 (1896). The attorney does not acquire the statutory charging lien until judgment is obtained, the attorney having no lien upon his client's cause of action. *Miedreich v. Rank*, 40 Ind. App. 393, 82 N.E. 117 (1907).

In the case *sub judice*, the Chapter XI petition was filed on November 17, 1976. The State Court judgment was entered on December 8, 1976.

Under Indiana law, Maley had no lien on the date the petition was filed. Despite the holding of the Court of Appeals, the correct analysis must apply the provisions of the Bankruptcy Act §67c(1)(B), 11 U.S.C. §107(c)(1)(B)

(1976), which defeats the alleged lien of Maley because said lien arose after the date of filing of the Chapter XI proceeding.

Certiorari should be granted because the Court of Appeals incorrectly interpreted Indiana law and failed to apply Section 67c(1)(B) of the Bankruptcy Act, the principles of which section have not been affected by the Bankruptcy Reform Act of 1978.

8. The decision of the Court of Appeals is erroneous in that it ignores the established principle that failure of counsel to comply with Bankruptcy Rule 215 and with the disclosure requirements of Bankruptcy Rule 219(a) and (b) is grounds for denying them compensation.

Bankruptcy Rule 11-22 makes Bankruptcy Rule 215 applicable in Chapter XI cases to employment of attorneys for the debtor-in-possession. Bankruptcy Rule 215 provides:

> (a) *Conditions of Employment of Attorneys and Accountants.* No attorney or accountant for the trustee or receiver shall be employed except upon order of the court. The order shall be made only upon application of the trustee or receiver....

Bankruptcy Rule 11-31 makes Bankruptcy Rule 219 applicable in Chapter XI cases. Bankruptcy Rule 219(a) provides in pertinent part:

> *Application for Compensation or Reimbursement.* A person seeking compensation for services, or reimbursement of necessary expenses, from the estate shall file with the court an application setting forth a detailed statement of (1) the services rendered and expenses incurred, (2) the amounts requested.

Bankruptcy Rule 219(b) states:

> *Disclosure of Compensation Paid or Promised to Attorney for Bankrupt.* Every attorney for a bankrupt, whether or not he applies for compensation, shall file

> with the court on or before the first date set for the first meeting of creditors, or at such other time as the court may direct, a statement setting forth the compensation paid or promised him for the services rendered or to be rendered in connection with the case, the source of the compensation so paid or promised, and whether the attorney has shared or agreed to share such compensation with any other person. The statement shall include the particulars of any such sharing or agreement to share by the attorney, but the details of any agreement for the sharing of his compensation with a member or regular associate of his law firm shall not be required.

In the instant case, neither Maley nor Cordes disclosed the existence of their employment contracts by affidavit as required by Rule 219(b) and Cordes failed to obtain an order authorizing his hiring and failed to file with the Bankruptcy Court a detailed statement of the services rendered by him together with his application for allowance as required by Bankruptcy Rule 219(a).

With respect to Cordes, the Bankruptcy Court found that it had not authorized his employment, that Cordes had failed to comply with the requirements of Bankruptcy Rule 219 and that, therefore, Cordes was not entitled to compensation from the estate except out of Maley's allowance. The Court of Appeals erroneously reversed the Bankruptcy Court's disallowance of compensation.

The general principle is established that when there is no compliance with rules under the Bankruptcy Act there is no right to compensation. It makes no difference whether the estate is benefitted, compensation will not be allowed. *Gochenour v. Cleveland Terminals Building Co.*, 142 F.2d 991 (6th Cir. 1944), *cert. denied* 323 U.S. 767 (1944); *Albers v. Dickinson*, 127 F.2d 957 (8th Cir. 1942).

As the Court stated in *Gochenour v. Cleveland Terminals Building Co.*, with respect to General Orders which the bankruptcy rules replaced, at 995:

> General Orders have the force of law . . . and cannot be

> by-passed by the creditors or their attorneys acting for the debtor without consent of the court. Since appellants do not bring themselves within the general order in question [requiring court approval for retention of attorneys for debtor], it is immaterial whether or not their services were beneficial....They are entitled to nothing here. (Citations omitted.)

The Court of Appeals should have addressed and applied that law to Cordes's request for fees.

The application of the principle to Maley's circumstance is equally appropriate and the Court of Appeals erred in not applying it. Maley applied to the Bankruptcy Court and was hired under a general retainer. He never filed the affidavit required by Bankruptcy Rule 219. He never disclosed to the court the existence of his alleged attorneys lien or his contingent fee agreement until November of 1979 when the Court ordered the condemnation proceeds invested subject to the "asserted liens." That was almost three years after the judgment was awarded.

Proper and orderly administration of all Chapter XI estates is dependent upon a firm application of Rules 215 and 219. The issue is one that is continuing and reoccurring. It has not been directly addressed by this Court and should be.

CONCLUSION

For all the foregoing reasons, this Court must not allow the decision below to remain as precedent, and Petitioner respectfully prays that a Writ of Certiorari to the Court of Appeals for the Seventh Circuit be granted.

Respectfully submitted,

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